CONSUMER MORTGAGE COALITION

December 24, 2009

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Truth in Lending Proposed Rule – Closed End Mortgage Loans
Docket No. R-1366

Dear Sir or Madam:

The Consumer Mortgage Coalition (CMC), a trade association of national consumer mortgage lenders, servicers, and service providers, appreciates the opportunity to submit these comments on the proposal by the Board of Governors of the Federal Reserve System (Board) to amend Regulation Z to improve the effectiveness of consumer mortgage disclosures, in connection with an application and throughout the life of a mortgage.

Overall, the Board's proposal would improve the clarity and effectiveness of disclosures in important areas. We strongly support the Board's efforts to improve these important disclosures and to help consumers make informed decisions. We appreciate that the Board "sought to ensure that the proposal would not reduce access to credit[,]"[1] which is especially important in the current environment when many consumers need to refinance their mortgagee loans. We further appreciate the Board's stated desire to ensure that disclosures under the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act of 1974 (RESPA) "are compatible and complementary, including potentially developing a single disclosure form" under both TILA and RESPA.[2] This is especially timely because the disclosure requirements under both sets of regulations are changing, and only coordinated disclosures will be useful to consumers.

We respectfully note some areas where the proposal could lead to adverse consequences, and make recommendations on how the Board might prevent or mitigate them. We suggest a number of technical clarifications to the definition of finance charge and to the disclosures. We comment on the regulatory burden of the proposed rule, which we believe

[1] 74 Fed. Reg. 43232, 43238 (August 26, 2009).
[2] 74 Fed. Reg. 43232, 43233 (August 26, 2009).

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the Board underestimates, and we suggest changes in one area where the proposed disclosure would entail extraordinary regulatory burden that we do not believe is outweighed by a consumer benefit. We also comment on the loan originator compensation proposal. Finally, we suggest a number of areas where the TILA and RESPA disclosures can be more closely coordinated.

I. ALL-IN APR

Background

One of the most significant proposed changes would be to include more items in the annual percentage rate (APR), the "all-in APR." As the Board explained:

> The Board believes consumers would benefit from having a disclosure that includes fees or charges that better represent the full cost of credit undiluted by myriad exclusions, the basis for which consumers cannot be expected to understand. In addition, having a single benchmark figure—the APR—that is simple to use should allow consumers to evaluate competing mortgage products by reviewing one variable. . . . Thus, the Board would retain the APR as a benchmark for closed-end transactions secured by real property or a dwelling but is proposing certain revisions designed to make the APR more useful to consumers.[3]

To this end, the Board proposes to include in the definition of "finance charge" a number of mortgage fees that currently are excluded from that definition. Because the APR is in part based on the finance charge, the proposed amendments would indirectly amend the APR.

Curtailed Credit Availability

We certainly support the intent of disclosing the cost of credit. We do note, however, one unintended consequence of amending the definition of finance charge, unrelated to the quality or effectiveness of consumer disclosures. That definition is the basis of other rules, in both federal and state laws that are not related to consumer disclosures. To the extent that the Board amends the finance charge definition in Regulation Z, it would also effectively change a number of other laws that refer to that definition. Those laws are designed to restrict the types of loans consumers obtain, as opposed to the disclosures they get in connection with all mortgage loans.

We are particularly concerned that the proposed change would inadvertently reduce the availability of consumer mortgage credit, which is the not the Board's intent.

TILA and Regulation Z effectively restrict Home Ownership and Equity Protection Act (HOEPA) loans, which include loans with an APR that exceeds the rate on comparable-term Treasury securities by a margin, as well as loans on which "the total points and fees

[3] 74 Fed. Reg. 43232, 43243 (August 26, 2009).

payable by the consumer at or before closing will exceed the greater of 8 percent of the total loan amount or [$579]."[4]

Most relevant here is the latter loan category, those with points and fees above a threshold. For these purposes, the proposal would amend the definition of points and fees to include "all items included in the finance charge, pursuant to § 226.4, except interest or the time-price differential."[5] The Board explains:

> This change would reflect the language of TILA more closely and is not meant to effect any substantive change to HOEPA's coverage.[6]

In addition, the proposed amendment to the definition of finance charge will affect the loans that meet the threshold for higher-priced mortgage loans (HPML). The threshold is loans:

> with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 or more percentage points for loans secured by a first lien on a dwelling, or by 3.5 or more percentage points for loans secured by a subordinate lien on a dwelling.[7]

Since the proposal would include new items in the finance charge, and because the APR is based on the finance charge, the proposal will increase the APR, making it more likely any loan will reach the HPML threshold.

The Board addressed the impact of its proposal on HOEPA loans and on HPML loans. It estimated the effect on APRs on first-lien loans using Home Mortgage Disclosure Act (HMDA) records and found that a relatively small number of loans would reach the HOEPA threshold if the proposal were in effect. It also estimated that, in the three states that use an APR threshold lower than the HOEPA APR threshold for first lien loans, the proposal would cause 2.5%, 4.0%, or 0% of the first-lien loans in those states to reach the state-law threshold.[8]

The Board also, using data from Lender Processing Services from 2006, estimated that about 3% of the first-lien loans in an amount from $175,000 to $225,000 that were below the higher-priced mortgage loan threshold would have exceeded it if the proposal had been effect at the time.[9]

HOEPA has two thresholds, one based on APR and the other based on points and fees. Reaching either threshold makes a loan a restricted high-cost loan. The Board concluded that the proposal would not have a large impact under the APR threshold. But it is also

[4] 12 C.F.R. § 226.32(a)(1)(ii). (The $579 limit will become effective January 1, 2010, after its annual adjustment.)
[5] Proposed § 226.32(b)(1).
[6] 74 Fed. Reg. 43232, 43278 (August 26, 2009).
[7] 12 C.F.R. § 226.35(a)(1).
[8] 74 Fed. Reg. 43232, 43244 (August 26, 2009).
[9] 74 Fed. Reg. 43232, 43244 (August 26, 2009).

important to consider the effect of the proposal on the HOEPA threshold, and similar state law thresholds, based on points and fees. The proposal does not address this issue. We do not believe the Board should implement an all-in APR without considering or addressing the effects of an all-in APR on the points and fees thresholds under the various state laws.

The proposal would cause more loans to reach the state points and fees threshold for high-cost lending restrictions in four ways.

First, many states – almost half of the states – have a points and fees threshold lower than the federal threshold. Adding new items to the definition of finance charge would make loans in these states more likely to reach the high-cost threshold even if the loan would not reach the federal HOEPA threshold.

Second, regardless of the threshold level, some states follow HOEPA rules, in whole or in part, for the method of calculating points and fees. In twelve states, all of the new items the Board proposes to include in the finance charge would be included in the state points and fees calculation. In an additional five states, treatment of new finance charge items is unclear. Because of the high litigation risk, in these five states creditors would need to assume the finance charge includes all the new items. This means that in seventeen states, every item the Board adds to the finance charge definition would count towards the state threshold for high-cost loans. In an additional three states, some costs would count towards the threshold while others would not.

This means that in twenty states, the all-in APR as proposed would make more loans reach the state points and fees threshold for restricted high-cost loans, regardless of whether the threshold is high or low.

Third, the finance charge as proposed would vary by state. Our research shows that the average finance charge would increase $2,500 per loan, nationwide. But we estimate that in New Jersey the increase would average almost $3,500, while in New York the increase would average over $4,500.

In New Jersey, the points and fees threshold is usually 4.5% of the loan amount. Assuming a loan principal of $200,000, the proposed definition of finance charge would bring the loan almost halfway to the points and fees threshold. ($3,500 is 1.75% of $200,000.)

In New York, the points and fees threshold is usually 5% of the loan amount. Assuming a loan principal of $200,000, the proposed definition of finance charge would, again, bring the loan almost halfway to the points and fees threshold. ($4,500 is 2.25% of $200,000.)

Many consumers prefer a loan with a number of points because in exchange they can get a reduced interest rate and a lower monthly payment. Yet in the two states illustrated, this option would be substantially curtailed.

Fourth, the proposed amendment to the definition of finance charge would reduce the total loan amount, which is the threshold level used in the HOEPA points and fees threshold. Reducing that threshold would make a loan more likely to reach the threshold. That threshold level is set as the amount financed determined under § 226.18(b) less certain financed costs.[10] Section 226.18(b) defines the amount financed to include the principal loan amount plus other amounts financed that are *not* part of the finance charge. The proposal to include many more items in the finance charge will therefore lower the HOEPA points and fees threshold.

Therefore, the proposal would cause many loans to reach state law points and fees thresholds. Since high-cost loans are widely regarded as predatory, extremely few lenders are willing to make them, whether under federal or state law. The proposal, then, would force creditors to restrict credit in many states. We believe this would be contrary to the intent of the proposal, would be harmful to consumers, and would directly counter the federal government's many efforts to increase credit in the mortgage market.

We do not believe curtailing credit availability is an appropriate manner in which to help consumers understand the terms of their credit.

<u>Other Unintended Disadvantages</u>

- ***Revised APOR Would Be Needed***

If the Board were to adopt an all-in APR, it would affect the HPML threshold as well as the HMDA rate-reporting threshold because both are based on the APR.[11]

Both the HPML threshold and the HMDA rate-reporting threshold are based on a comparison of the APR to the average prime offered rate (APOR). Including more costs in the APR without similarly amending the APOR would alter both thresholds. The intent of the all-in APR is to improve the effectiveness of the APR disclosure. We do not believe the Board intended to amend the APR-based thresholds.

Altering the HMDA rate-reporting threshold would make HMDA data less useful because comparisons of data before and after the all-in APR effective date would be distorted by inconsistent reporting requirements, for economically equivalent loans. We do not believe distorting the HMDA data is appropriate when the goal is to improve consumer disclosures.

To avoid having an all-in APR amend the HPML threshold and the HMDA rate-reporting threshold, neither of which were the Board's intent, revised APORs would be necessary. Even if the Board were somehow able to accurately measure and track fees and incorporate them into revised APORs, it would be faced with a new problem. Since mortgage fees vary substantially from state to state, the APORs would need to be either set nationally and therefore be inaccurate, or would need to vary geographically. Neither result should be the effect of an effort to improve APR disclosures.

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[10] Comment 226.32(a)(1)(ii)-1.
[11] 12 C.F.R. § 226.35(a)(1); 12 C.F.R. § 204.3(a)(12)(i).

A combination of the difficulties in including fees in APORs, and the credit curtailment and distortion of HMDA data without revised APORs, together are another reason we believe the Board should not adopt the proposed all-in APR.

- ***Increased Mandatory Waiting Periods***

The all-in APR would also result in a number of redisclosures before loan consummation as the cost of expanded number of items included in the APR change. Each redisclosure would require a new three-day waiting period before a loan could close. Consumers will undoubtedly be annoyed, inconvenienced, and sometimes economically harmed from mandatory waiting periods.

Conclusion

For these reasons, we are unable to support the proposal to eliminate the current exclusions from the definition of finance charge, in proposed §§ 226.4(c)(7) and 225.4(g). We believe the Board should not implement the all-in APR, as proposed.

II. ALL-IN APR ALTERNATIVES TO MITIGATE LENDING CURTAILMENT

While we believe the Board should not implement its proposed changes to the definition of finance charge because they would reduce credit availability, we support the Board's underlying goal of improving consumer's ability to understand the cost of mortgage credit.

However, the proposal would not accomplish this goal, and would come at the cost of restricting the availability of consumer mortgage credit to creditworthy families, delaying closings, and distorting HMDA data. For these reasons, we cannot support the proposed all-in APR approach to making disclosures more accurate.

Should the Board decide to finalize an all-in APR despite its flaws, we recommend a number of changes that would support the intent of the all-in APR but would help reduce some of the disadvantages.

Include Settlement Costs in the APR but not in the Finance Charge

The Board's intent is to make the APR a more meaningful disclosure for consumers. The proposal amends the definition of finance charge rather than the definition of APR, but this would have a number of disadvantages, discussed above, unrelated to the APR disclosure, or the quality of any disclosures.

A better approach would be to amend only the APR. The costs that are currently excluded from the definition of finance charge that the Board proposes to include could be included for purposes of the APR calculation but continue to be excluded from the finance charge for other purposes. This would meet the Board's goal of an improved APR disclosure, while avoiding some of the unrelated problems caused by amending the definition of finance charge.

Include Settlement Costs In The Finance Charge, With A RESPA-Based Cap

Creditors identify in a RESPA good faith estimate (GFE) the estimated cost of third-party settlement services. The Board's proposal would include third party costs in the finance charge and APR. This would have the effect of subjecting creditors to liability for changes, beyond extremely small tolerances, for third-party costs.

The Board has requested comment on whether it should increase the finance charge tolerance in light of the proposal to include more third-party charges in the finance charge.[12] The Board suggested the possibility of increasing the finance charge tolerance to $200.[13]

The proposed definition of finance charge would create another area of interplay between the TILA and RESPA rules. That is, the proposed expanded Regulation Z definition of finance charge would now include a number of third-party charges, but RESPA § 8 does not permit lenders to guarantee those costs to consumers. That means creditors will be accountable, under TILA, for third-party charges that are governed by the RESPA § 8, which effectively prohibits guaranteeing those fees.

We believe the best approach for consumers would be to permit settlement service providers to guarantee to consumers the costs of closing their mortgage loans. This would enable packagers of settlement services to use their purchasing leverage to lower closing costs for consumers. It would also make certain that consumers learn with certainty the costs of their loan very early in the application process, a major goal of both RESPA and TILA rules. This would, however, require relief from RESPA § 8 liability, which RESPA rules do not currently provide. The unfortunate effect is that consumers' closing costs are higher than they need to be.[14]

Until packagers are permitted relief from RESPA § 8, lenders will need to estimate third party charges rather than guarantee them. To handle the inevitable incorrect estimates that lenders give consumers about the cost of third party charges, RESPA rules establish a 10% tolerance above the estimated costs, for lender-required settlement services when the lender selects the provider or when the consumer selects the provider from a lender's written list of providers.

Because of RESPA § 8, incorporating third party charges into the Regulation Z definition of finance charge would make the TILA-based tolerance inappropriate. A $200 tolerance

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[12] 74 Fed. Reg. 43232, 43246 (August 26, 2009).
[13] 74 Fed. Reg. 43232, 43246 (August 26, 2009).
[14] According to a HUD analysis in 2002, if lenders were permitted to guarantee settlement costs to consumers, the result would be a $10.3 billion in total savings to consumers.[14] This is almost $1,000 per loan. Similarly, in a joint report to Congress by the Board and HUD in 1998, the two agencies found that guaranteed closing packages would result in savings to consumers. The Report is available here: http://www.federalreserve.gov/boarddocs/rptcongress/tila.pdf. *See* Appendix E.

simply would not cover even the most routine fluctuations in third-party charges that lenders can neither predict nor control, and that they are not permitted to guarantee to consumers.

Short of RESPA § 8 relief, if the Board does finalize an expanded definition of finance charge, we recommend that it cap the amount of third party charges that are included in the finance charge, based on the RESPA tolerances. This would include in the finance charge the costs of third-party settlement services listed in GFE Blocks 3, 4, 6, and 7, that would not be paid on a comparable cash transaction, as the lesser of either the actual charge (after taking into consideration any cure of an exceeded tolerance) or the charge as listed on the GFE plus a 10% tolerance as provided in 24 C.F.R. § 3500.7(e)(2).

This approach has several advantages.

- It would reflect the true cost of credit. A cost would exceed the RESPA tolerance when the borrower shops for and selects a service provider that is more expensive than one the lender identified on the GFE, but this extra-expensive service is not an accurate cost of credit because the borrower could have selected a less expensive service provider. Presumably the borrower opted to pay a higher cost because it includes some unrelated extra service or benefit.

- It would reduce regulatory burden on lenders. Some charges are for service providers that a borrower selects, while the lender does not require the service, and does not select or identify the provider. In this case, the regulatory burden on the lender of knowing the actual charges would be extremely high, while the borrower is fully aware of the costs of services the borrower shops for and selects.

- It would enhance borrower's shopping ability and power. The proposal would put on creditors the burden of knowing the costs of third-party charges, within an extremely small tolerance. The only feasible way for creditors to know the charge would be to limit consumers to third parties whose costs the creditor can know in advance. It will be easier, and will greatly reduce litigation risk, for creditors to require consumers to use large national or regional service providers. Smaller or local service providers will be excluded even if they have better prices. Consumers would have fewer shopping options.

- It would reduce the number of loans inappropriately classified as high-cost loans or as HPML loans. If a consumer selects an expensive service provider, and if that extra cost were included in the finance charge, the loan would be more likely to reach the high-cost or HPML threshold. The consumer's selection of a settlement service would be irrelevant to the policy reasons behind the restrictions on high-cost or HPML loans. Rather, the consumer may select an expensive service provider for completely unrelated reasons – the service provider may be a friend, may have a convenient location, or may include in the charge unrelated services that are of value to the consumer. These extraneous matters should not affect whether a loan reaches the high-cost or HPML thresholds.

- It could decrease the number of additional waiting periods and delayed loan closings. Because the charges included in the finance charge would not exceed the amount disclosed in a GFE plus 10%, the borrower's decision to select a more expensive service provider would have a limited affect on the accuracy of the TILA disclosure, and would therefore be less likely to require a corrected disclosure and a new waiting period.

- It would help coordinate the TILA and RESPA rules, thereby increasing consumers' ability to understand and benefit from the disclosures, while reducing regulatory burden.

Exclude Points and Fees From § 226.32 Definition

Another approach to preventing an unintended curtailment of credit while improving the APR's accuracy would be to: (i) define points and fees in § 226.32(b)(1) to retain the current finance charge exclusions, for purposes of § 226.32, even though those amounts would still be finance charges, and (ii) retain the incorporation into the definition of the total loan amount under Comment 226.32(a)(1)(ii)-1 the finance charge exclusions currently stated in § 226.18(b).

This approach is consistent with TILA's approach to high-cost loans. TILA excludes, for high-cost loans, many real estate fees from the definition of points and fees. TILA defines points and fees, for purposes of high-cost loans, to exclude real estate-related fees, including government recording fees, when those fees are reasonable and are paid to a third party and not to the creditor or the creditor's affiliate.[15]

Excluding real estate-related fees from the § 226.32(b)(1) definition would permit the Board to adopt the all-in APR it proposes without unnecessarily curtailing credit, especially in those states that use a low points and fees threshold in restricting high-cost loans.

III. CLARIFICATIONS OF FINANCE CHARGE

Should the Board finalize its proposed amended definition of finance charge, we request clarification on a number of issues.

Special Rule for Closing Agent Charges

The proposal would exclude several items from the special rule for closing agent charges, § 226.4(a)(2). The result is that all fees a closing agent charges, or fees for another party the closing agent hires, would be included in the finance charge. Closing agents sometimes charge borrowers fees that are excessive, or that are both unrelated to the loan and were not requested by either the creditor or the consumer.

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[15] 15 U.S.C. § 1602(aa)(4)(C).

To prevent surprise charges to consumers, and to avoid increasing creditors' liability for uncontrollable closing agent charges, we suggest the Board require closing agents to disclose to creditors all their charges, including those for third parties they hire, eight business days before consummation. This would provide sufficient time to accommodate the three-day waiting period after a final corrected disclosure before consummation.

Voluntary Credit Insurance Premiums, and Voluntary Debt Cancellation or Debt Suspension Fees

The proposal would include in the finance charge premiums for voluntary credit insurance, and premiums for voluntary debt cancellation coverage or debt suspension fees. As a practical matter, this would make it very difficult to continue to offer these products to consumers. It would be better to continue to exclude these charges from the finance charge, but instead:

- Prohibit charging the premium or fee as a single cost at or before closing.
- Require the fee to be charged with periodic loan payments.
- Permit the consumer to be able to cancel coverage at any time.
- Require that a consumer's cancellation must terminate all future obligations to pay premiums or fees.

We also recommend amendments to the proposed Model Clauses H-17(C) and H-17(D) for credit insurance and debt cancellation or suspension. These model clauses state that "If you have insurance already, this policy may not provide you with any additional benefits." This is not necessarily true, and could be misleading. It would be true only in the highly unusual case where a consumer has preexisting credit insurance, debt cancellation, or debt suspension protection coverage that would cover the loan to at least the coverage level, and in at least the same circumstances as, the new product.

Further, the statement may lead consumers to believe that if they have mortgage insurance or life insurance that the new product may not provide any benefits that the mortgage insurance or life insurance do not provide. This is not true, so we believe this is not an appropriate disclosure.

We also recommend removing the reference in the Model Clauses to employment status, as the creditor may be unable to verify the consumer's employment status at the time of providing the disclosure.

We also recommend removing the command "STOP" from the disclosure. The next sentence, "You do *not* have to buy this product to get this loan," makes the same point.

Hazard and Flood Insurance

We support the proposal's exclusion from the finance charge of premiums for hazard insurance. A homeowner would pay for hazard insurance in a comparable cash transaction. Additionally, the amount of hazard insurance coverage the homeowner selects will vary by borrower preferences regarding levels and types of insurance coverage, which is unrelated to a mortgage loan.

We recommend that, for the same reasons, flood insurance premiums be excluded from the finance charge in all cases, regardless of whether the borrower chooses the flood insurance provider. Otherwise, lenders would have an inappropriate incentive to discourage borrowers from obtaining flood insurance.

The proposal would require creditors to treat insurance available through the creditor's affiliate as available from or through the creditor, and thereby require disclosure of the premium and, if shorter than the loan term, the insurance term. We support this. However, we request clarification that the affiliate may deliver the required disclosures.

We also request clarification that proposed § 226.38(j)(4), which would require a disclosure that the consumer may obtain property insurance from any insurer acceptable to the creditor, also refer to the disclosures required to exclude property insurance available from or through the creditor from the finance charge.

Seller Points And Relocation Benefits

Points and fees that a seller pays should not be included in the finance charge because the seller would also pay them on a comparable cash transaction. Economically to the seller and buyer, they are part of the sales price of the property. If the seller did not pay them, the buyer would pay a lower price to purchase the house. In a comparable cash transaction, the seller would not pay the buyer's loan points or fees, but would instead receive a lower price, other things being equal.

We further recommend that the final regulation clarify that amounts an employer pays to relocate an employee are excluded from the finance charge because the consumer does not pay these costs. They are not part of the cost of consumer credit.

Charges for Lien Discharge or Resubordination

We recommend that the cost of discharging a lien or of resubordinating a lien be excluded from the definition of finance charge. On a refinance, the existing creditor may charge a fee to prepare and record a release of that creditor's lien or a resubordination of the lien.

The recording cost will vary by the length of the document, and will also vary by geographic area. We do not believe that including costs that vary for reasons unrelated to the new loan in the APR would serve the Board's intent of improving the usefulness of the APR disclosure to consumers.

Excluding these costs from the finance charge would not affect the consumer's ability to shop for loans because the consumer would need to pay the same costs regardless of which creditor the consumer selects.

Conversion or Modification Fees

Fees charged to convert a loan from an adjustable rate to a fixed rate, or to modify a loan, should be excluded from the definition of finance charge because at origination the creditor cannot know whether the consumer may convert or modify the loan. The disclosures should be made assuming the consumer pays the loan according to the legal obligation.

Required Property Completion or Repairs

If a property was or will be newly constructed, the creditor will need to ensure the building is fully and properly completed. Construction and repair costs may be needed. These costs should not be included in the definition of finance charge, for several reasons:

- The consumer would pay them on a comparable cash transaction.
- The costs would in many cases push the loan over the threshold for HOEPA or state law high-cost loans, preventing the loans from being made.
- The costs are difficult to predict, and would be unknown at the time of loan application.
- Including these costs in the finance charge would not improve the consumer's ability to shop for a loan, but would distract the consumer's attention from loan costs.
- Including these costs in the finance charge would encourage creditors avoid repairs that would benefit the homeowner, may protect the consumer's health and safety, and could prevent damage to the surrounding neighborhood.

Payoff of Existing Liens or Debts

The cost of payoff of an existing lien should not be included in the definition of a finance charge. The property may have, for example, a tax lien that the lender requires to be discharged. Or, the consumer may apply for a debt consolidation loan, or may be required to pay off other debts at the time the new loan is underwritten. These costs are unrelated to the mortgage loan. They should not be included in the definition of finance charge for the following reasons:

- Including these costs in the finance charge would not improve the consumer's ability to shop for a loan, but would distract the consumer's attention from loan costs.
- The costs would in many cases push the loan over the threshold for HOEPA or state law high-cost loans, preventing the loans from being made.
- Without the new mortgage loan, the consumer may be unable to pay off the debts or liens, possibly leading to an unnecessary and avoidable loss of the home.

Government Recording Fees

We recommend that the Board retain the exclusion of government recording fees from the definition of finance charge. Since these fees are set by governmental entities, the difference between these fees from one creditor's loan to another creditor's loan is trivial. Including such fees in the finance charge will not enhance the consumer's ability to shop.

Furthermore, the recording fees in some states are substantially higher than others. In higher cost states, including these fees may cause the loan to exceed HOEPA or state law high-cost loan APR thresholds, or points and fees thresholds, or both. This would not serve the Board's intent of improving the effectiveness of the APR disclosure.

Clarification About Fees Charged in Comparable Cash Transactions

Charges payable in a comparable cash transaction are excluded from the finance charge. Proposed comment 226.4(g)-3 clarifies that the cost of recording the deed that transfers title to the property from the seller to the buyer is excluded from the finance charge. We request that the following items be added to this comment and likewise excluded from the finance charge because they are paid in comparable cash transactions:

- Fees for preparing the deed and other documents related to the purchase of the property. (The Board's Section-By-Section analysis of the proposal describes these as included in the finance charge.[16])
- Real estate broker's fees.
- Fees of the borrower's attorney.
- Escrow agent charges.
- Fees for services required under the purchase and sale agreement with the seller.

It would be particularly helpful if the Board and the Department of Housing and Urban Development (HUD) would coordinate so that these charges were listed in a separate block on the GFE from the charges that are included in the finance charge.

Post-Closing Optional Services

Fees that are part of the original loan agreement are included in the definition of finance charge without regard to whether they are paid at closing or later, such as interest. Sometimes, though, after a loan closes, the loan servicer may provide services to the consumer that are outside the loan agreement. The cost of these optional services should be excluded from the finance charge. At origination, the creditor cannot know what they may be at some future time.

Voluntary and Optional Fees Incident to the Extension of Credit

Creditors may sell products or services to a consumer in addition to a mortgage loan. It is important that the costs of services that are only tangentially related to the loan, or that the creditor might not know about at all, not be included in the finance charge.

For example, a bank making a mortgage loan may cross-sell the borrower a checking account with a monthly fee. It is not clear whether the fact that the cross-sale opportunity arose out of the mortgage application makes the checking account charge a voluntary charge incident to the extension of credit

[16] 74 Fed. Reg. 43232, 43247 (August 26, 2009).

Or, a consumer, prior to closing on a new loan, may arrange with a bank, other than the creditor, for automated payments on the mortgage loan, but the lending bank may be unaware of this. It is not clear whether, if the non-lender bank charges a fee for that service, the fee is a finance charge.

Moreover, including the cost of optional products or services in the finance charge and APR would distort the usefulness of the finance charge and APR disclosures as shopping comparison or consumer education tools. It would cause the finance charge and APR to fluctuate based on matters unrelated to the loan, such as what non-loan services a creditor offers or a consumer selects.

If the Board does require additional disclosures or includes the cost of optional services in the finance charge, we recommend that the service be deemed "incident to" the loan, and therefore subject to the requirements, only if the creditor requires the consumer to purchase the service and if the consumer contracts for the service at or before consummation.

Payments into Escrow

Proposed § 226.4(g) excludes, with some exceptions, certain real estate-related charges from the definition of finance charge on closed-end transactions secured by real property or a dwelling. The Board's Section-By-Section Analysis of the proposed rule explains that the finance charge will exclude "amounts required to be paid into escrow or trustee accounts if the amounts would not otherwise be included in the finance charge."[17] This makes sense because property insurance premiums and property taxes are unrelated to mortgage credit, and are paid on comparable cash transactions. Also, including property taxes in the finance charge would cause APRs to vary geographically on identical loans. Moreover, including taxes in the finance charge could cause a loan to well exceed the HOEPA or HPML threshold, or a similar state threshold, depending on the wholly irrelevant fact of when a tax payment is next due.

If a loan closing is scheduled shortly before a property tax payment is due, the property tax payment to be made into the escrow account would bring the loan much closer to the HOEPA or HPML threshold, particularly in states with high property taxes. Property tax rates, and the timing of when taxes are due, should be entirely irrelevant to HOEPA and HPML thresholds. Property taxes are due regardless of whether the consumer has a mortgage.

Proposed § 226.4(g) does not include a reference to § 226.4(c)(7), escrowed items that are not otherwise included in the finance charge. We strongly urge including such a reference so that the timing and amount of property tax payments does not affect the HOEPA and HPML thresholds.

[17] 74 Fed. Reg. 43232, 43247 (August 26, 2009).

Premiums and Rebates

Proposed comment 226.28(e)(5)(iii)-2, regarding disclosure of the loan principal amount, states that when a creditor offers a premium or when a third party pays some of the cost of credit or offers a buy down, the disclosure of the premiums or buy downs must be reflected in accordance with the terms of the legal obligation between the creditor and consumer.

➢ ***Preclosing Credits***

Where the premium will be paid after the loan is consummated, it should be relatively clear whether the premium is part of the legal obligation. However, creditors often provide marketing credits to reduce closing costs that are not documented in the note or other documentation evidencing the loan because those credits are applied at or before consummation. We recommend a clarification that amounts paid by the creditor at or before consummation may be used to reduce the finance charge.

➢ ***Rate Reduction Mortgages***

Rate reduction mortgages provide that if the consumer makes a certain number of timely payments, the rate on the loan will decrease. These programs are generally offered to borrowers who have less than excellent credit as an incentive to make timely payments. We request a clarification on whether the disclosures should assume that timely payments will be made and reflect the decrease.

IV. DISCLOSURES AT OR BEFORE CONSUMMATION

Scope

We support the proposal to require disclosures for all closed-end consumer loans secured by real property or a dwelling, with the following exceptions.

➢ ***Vacant Land***

We believe it would be preferable to permit creditors the option of providing disclosures on loans secured by vacant land under either the general closed-end credit rules or the new rules applicable to closed-end loans secured by a dwelling. Because loans on vacant land are not secured by a dwelling, there does not seem to be a need to *require* all of the same protections that apply to loans secured by a dwelling. As a practical matter, creditors may find it easier to apply the same rules, whether the property is vacant or has a home on it. Therefore, we believe creditors should have a choice.

But if a loan is secured by vacant land, if a creditor were to make disclosures as for a loan secured by a consumer's dwelling, certain adjustments would be advisable.

- Proposed § 226.38(b)(5) exempts construction loans and temporary bridge loans from the requirements of § 226.38(b)(2) and (b)(3) to compare the loan's APR to the

APOR. That exemption should be extended to loans secured by vacant land, because the rates for loans on vacant land are substantially different that the rates for conforming, owner occupied loans. Comparing the APR and APOR would result in a misleading disclosure, and therefore should not be required.

- On a loan secured by vacant land, creditors should be permitted to revise the security interest disclosure required by § 226.38(f)(2) so that it does not refer to the possible loss of "the home" because there is no home on vacant land.

➢ ***Loans Secured By Personal Property That is a Dwelling***

The Board's proposal would require creditors to provide certain disclosures for all closed-end transactions secured by real property or a dwelling, not just principal dwellings. This would greatly increase creditor's litigation risk, and thereby the cost of consumer credit, while there is no reason to believe that such loans have been the subject of inappropriate lending practices. Extending Regulation Z to these loans could reduce the availability of credit, and we therefore recommend against it.

Preapplication Disclosures

The Board proposes Model Forms for preapplication disclosures, which we believe are useful and clear. We recommend some minor adjustments.

➢ ***Brokers Should Be Able To Provide Disclosures***

We recommend that brokers be permitted to provide the forms. This would help get the disclosures to consumers quickly.

➢ ***"Key Questions To Ask About Your Mortgage"***

The Board proposes a new form, Key Questions to Ask About Your Mortgage, listing seven questions and answers. We suggest the following revisions to this form.

Question 1. The answer to this question indicates that on ARMs the interest can go up or down "after a short period." However, that may not be accurate. The rate may be fixed for a period of years, perhaps five or ten years. We suggest this disclosure be revised to delete the language in ~~struck through~~ and add the language in **bold**.

> *If you have an adjustable rate mortgage (ARM), your interest rate can go up or down ~~after a short period~~. This means that your monthly payment could increase.* ***On some ARMs your initial rate and payment may be in effect for only a short period.***

Question 2. The answer to question 2 indicates that payment may increase because "your property taxes or insurance premiums increase." However, the consumer's property taxes or insurance premiums may increase regardless of what mortgage loan the consumer chooses or whether the consumer has a mortgage at all. To be most clear, we suggest separating the loan payment from the taxes and insurance, as follows:

> *This increase could be because you have a lower introductory interest rate~~, your property taxes or insurance premiums increase,~~ or because in the beginning your monthly payment only covers the interest on the loan, and not the principal amount.* ***Your payments for property taxes or insurance premiums could increase.***

Question 3. Generally, the questions listed in the *Key Questions To Ask About Your Mortgage* are asked and answered in the same format in subsequent disclosures. However, Question 3, "Will my monthly payments reduce my loan balance?" becomes "Will any of my monthly payments be interest-only?" in subsequent disclosures. We suggest that this question on the *Key Questions To Ask About Your Mortgage* form use the same language as used on subsequent disclosures.

Additionally, whether the loan requires payment of principal has an effect on the consumer's equity, but decreases in the market value of the home may have an even greater effect. We suggest adding the language in bold to the last sentence of the answer: "As a result, if you have this type of loan, you may not build any equity in your home **even if your home does not decrease in value.**

Making both changes, Question 3 would read,

> *Will any of my monthly payments be interest-only?*
> *Some loans let you pay only the interest on your loan each month. These payments do not pay down the amount you borrowed. As a result, if you have this type of loan, you may not build any equity in your home even if your home does not decrease in value.*

Question 4. For the same reason discussed above under Question 3, we suggest adding language to the last sentence of the answer:

> This could cause you to lose equity in your home over time **even if your home does not decrease in value**.

Question 5. This question covers prepayment penalties. It alerts consumers that "Some loans charge you a large fee if you pay off your loan, refinance it, or sell your home within the first few years of the loan. The penalty fee could be thousands of dollars."

While these are true statements, we suggest alerting consumers to an additional fact, that they have a decision to make. They need to decide whether to select a loan with a prepayment penalty and a lower loan cost, or a loan with no prepayment penalty and a higher cost. We believe consumers should be aware of the tradeoff so that they can ask appropriate questions and make the most informed decisions. We suggest revising the disclosure to state:

Some loans charge you a large fee if you pay off your loan, refinance it, or sell your home within the first few years of the loan. The penalty fee could be thousands of dollars. ***These loans may have lower costs than loans with no prepayment penalty.***

Question 7. This question, "Will I have to document my employment, income and assets to get this loan?" in subsequent disclosures becomes "Will my loan have a higher rate or fees because I did not document my employment, income or other assets?" in subsequent disclosures. We suggest that this question on the Key Questions form use the same language as used on subsequent disclosures.

- ***"Fixed vs. Adjustable Rate Mortgages"***

The Board proposes a new form, *Fixed vs. Adjustable Rate Mortgages*. We suggest the following revisions to this form.

The column of the form describing ARMs contains the following sentence: "However, both the rate and payment can increase very quickly." This statement is not accurate for hybrid ARMs that have many years until the first adjustment. We recommend revising this sentence to add the bold language as follows:

However, ***on some ARMs*** *both the rate and payment may increase very quickly.*

Subsequent disclosures distinguish between fixed rate loans and step rate loans and have additional requirements for fixed rate balloon loans, but this disclosure appears to tell the consumer that if the rate is fixed then payments will stay the same for the life of the loan. We suggest adding the bold language to the first sentence of the first paragraph of the disclosure:

A traditional fixed rate mortgage ***with equal monthly payments throughout the life of the loan*** *is a safe choice for many borrowers.*

We further suggest that description in the Fixed Rate Mortgages column be revised to address this issue and the risks of a fixed rate mortgage:

With a fixed rate mortgage, the interest rate and monthly payment ***usually*** *stay the same for the entire loan term.* ***However, the interest rate and monthly payment often are higher than the initial rate and payment on an ARM.***

- ***ARM Program Disclosures***

ARMs Where the Initial Rate is Not Determined Using the Index or Formula That Applies to Rate Adjustments

On ARM programs where the initial interest rate is not determined using the index or formula that applies to later rate adjustments, the creditor will often not know, when giving the program disclosure, whether the initial rate will be discounted from the fully indexed rate, will be the same as the fully indexed rate, or will be a premium over the fully indexed rate. This is precisely because the rate is not set using the formula that will apply to later rate adjustments.

Additionally, borrowers often have the choice of paying discount points and obtaining a lower initial interest rate, or taking a higher initial interest rate and receiving a credit towards closing costs. Whether a borrower chooses to pay discount points to get a lower initial rate or chooses to pay a higher initial rate to receive a credit, the fully indexed rate would not be affected. Because the disclosure precedes the loan application, the creditor does not know, when giving the program disclosure, what choice the borrower will make and whether the initial rate will be a discounted or premium rate. Further, changes in the index value after the disclosure and before consummation could change whether the initial rate was a discounted or premium rate. That is, it is too early in the loan application process to make an accurate, transaction-specific disclosure.

We recommend that the Board require a disclosure that better informs consumers about the nature of the transaction. We recommend that the Board revise the Introductory Period box to state:

> *The interest rate will stay the same for [length of time].*

A statement could be added either in the Introductory Period box or in the Index/Formula box to state that:

> *During the initial period the interest rate may be based on the index [shown below] plus a margin or could be a higher or lower amount. Ask us for more detail.*

This would be more informative to consumers, and would give them all the information then known.

Other Loan Programs Presenting Risks

We believe it would be beneficial to require pre-application loan program disclosures that describe the risks of the loan features identified in the *Key Questions To Ask About Your Mortgage* form. This would include loans other than fixed rate, fully amortizing loans,

The disclosures should describe the risks but, because the disclosure would precede the loan application, the disclosures could not be transaction-specific. In many cases, creditors and mortgage brokers are already required by the Nontraditional Mortgage Guidance adopted by both federal and state regulators to provide information about risks. These disclosures can help consumers identify the type of loan they want early in the process.

- ***Disclosure Timing Requirements For "Key Questions To Ask About Your Mortgage" and "Fixed vs. Adjustable Rate Mortgage"***

The proposal includes two model forms, *Key Questions To Ask About Your Mortgage* and *Fixed vs. Adjustable Rate Mortgage*, that describe information similar to that in the "Summary of your loan" section in the new GFEs. The Board proposes to require creditors to deliver these forms at application, although RESPA rules require delivery of the GFE within three days of receiving an application. All of these disclosures should be required within three days of application because this would coordinate the RESPA TILA rules.

We believe many or most creditors and brokers will provide the two model forms earlier, and will post them on their websites, as will real estate agents, housing counselors, and many others. However, we believe the disclosure timing rules under RESPA and TILA should be as consistent as possible to reduce the cost of complying with both sets of rules. We recommend that a creditor or broker be required to provide these two forms within three days of receipt of an application,

If the Board believes consumers need these disclosures sooner, the Board and HUD could post the model forms on their websites. This would make the forms very widely published and available, while reducing regulatory burden.

TILA Timing and Redisclosure Requirements

- ***Early TILA Disclosure***

Definition of Application

The Proposal's revised Comment 19(a)(1)(i)-2 provides that creditors may, in determining whether an application has been received, rely on RESPA and Regulation X even for a transaction not subject to RESPA. We recommend that this comment be further revised to state that for such transactions, the creditor may also determine whether an application has been received by relying on the Equal Credit Opportunity Act (ECOA) and Regulation B. This would have no material effect on consumers, yet would reduce regulatory burden.

General or Precise Definition of "Business Day"

Both the current regulation and the proposal require that early TILA disclosures be mailed or delivered within three "general" business days after application. "Precise" business days are all calendar days except Sundays and the legal holidays specified in 5 U.S.C. § 6103(a). "General" business days are defined as days that "the creditor's offices are open to the public for carrying on substantially all of its business functions." In most instances, creditors will have far fewer employees working on Sundays and legal holidays and would have difficulty preparing disclosures on those days. However, because the public may be able to contact the creditor on those days, or possibly close a loan on those days, the current rule creates unnecessary uncertainty as to whether the creditor is "open."

Comment 226.2(a)(6)-1 states that indicators of when a creditor is open for substantially all of its business include the availability of personnel to make loan disbursements, open new accounts, and handle credit transaction inquiries. This is a difficult standard to apply because creditors often have personnel available to handle inquiries and at all hours, and have website capability to handle many functions at all times.

In contrast, a creditor's staff that prepares the disclosure is normally only available during standard, weekday, non-holiday business hours.

For these reasons, we recommend that the creditor be deemed to have delivered the early TILA disclosure on a timely basis if the early TILA disclosure is mailed or delivered within three "general" business days. We further recommend that creditors should not be required to count Sundays and Federal holidays as business days, regardless of how "open" the creditors are on those days.

- ***Guidance on Whether Revised TILA Disclosure May Reflect Current Estimates of Charges or May Reflect Charges Shown on a GFE***

The final RESPA rule and HUD's implementing Frequently-Asked-Questions (FAQs) indicate that a revised GFE should not increase the estimates for settlement charges from the estimates for those charges in the initial GFE, unless justified by changed circumstance or a borrower-requested change. This is the case even if the creditor may have subsequently obtained information showing that the fee is higher than initially estimated.

For example, assume that fees subject to the 10% tolerance were initially estimated at $2,000 but are now estimated at $2,100, yet there has been no changed circumstances warranting a revised GFE with an increase in those estimated costs. Since the comparison of GFE fees to actual fees on page 3 of the HUD-1 settlement statement bases the tolerance calculation on the amounts disclosed on the GFE, the amount disclosed on the revised GFE should continue to be $2,000, so that borrower can see that the actual charge of $2,100 is within tolerance.

We request a clarification to Comment 226.17(c)(2)(i)-1 that the creditor may estimate the amounts of fees for TILA purposes using either:

- The amount of the fees based upon information reasonably available at the time the TILA disclosure is made (the $2,100 amount in this example); or

- Amounts shown on GFE plus 10% ($2,200 in this example) even though Regulation X may require any revised GFE to disclose a lower amount.

- ***Final TILA Disclosure***

  Use of Estimates

The Proposal would limit the use of estimates in the final TILA disclosure to certain disclosures affected by escrowed taxes, insurance premiums, and mortgage insurance premiums.

- Limit on Consumer's Ability to Float Rate Until Closing

  Many creditors allow borrowers to choose to continue to float the interest rate up until closing rather than lock the rate earlier. The proposed limits on the use of estimates will effectively require borrowers to have their rates locked more than a week before consummation. We defer to the Board's judgment on whether it is in the consumer's interest to remove the ability to float the rate until closing in exchange for greater certainty in the final TILA disclosure.

- Per Diem Interest

  Since closing are sometimes postponed, we recommend a clarification to Comment 226.17(c)(2)(ii)-1. This comment states that disclosures affected by per diem interest are considered accurate if they are prepared on information known at the time the disclosure is prepared, even if they are not labeled as estimates. We recommend clarifying that this also applies to per diem interest disclosures in the final TILA disclosures, so that those disclosures are not deemed inaccurate simply because of a delayed closing.

- Disclosures Affected by Changes in Settlement Charges

  Required disclosures that are affected by changes in settlement charges but which may not be estimated under the Board's proposal include the Total Settlement Charges as required to be disclosed on the HUD-1, the Interest and Settlement Charges (Finance Charge) disclosure, the APR disclosure, and the Amount Financed disclosure.

  While the Board's proposal does not conflict with the tolerance and timing rules of Regulation X to the extent that it would be possible to comply with both the Regulation Z and Regulation X requirements, the Proposal is certainly inconsistent with and duplicative of Regulation X requirements. We recommend that estimates of settlement charges be permitted on the final TILA disclosure if they are consistent with Regulation X requirements.

  As the Board recognizes, requiring disclosures that are not estimates will require settlement costs to be finalized as much as a week before consummation.[18] Since the creditor cannot necessarily predict third-party closing costs, the creditor will need to have the closing agent provide the Total Settlement Charges and information sufficient to determine the Finance Charges included within the Interest and Settlement Charges at least eight business days prior to closing. The

[18] 74 Fed. Reg. 43232, 43260 (August 26, 2009).

Board also recognizes that most creditors provide either a GFE or HUD-1 according to Regulation X timing rules to satisfy the Itemization of Amount Financed requirement, but the Board's proposal would not permit using the HUD-1 to fulfill this requirement unless it is delivered with the final TILA disclosure.

If the Board intends to have closing agents finalize settlement costs and prepare the final HUD-1 so that a final TILA disclosure will not require any estimates, then the regulation should explicitly require the closing agent to do so.

➢ ***Corrected Final TILA Disclosure***

Alternative 2 With a Modification

The Board proposes two alternatives regarding the need to correct a final TILA disclosure due to changes after a final disclosure. Alternative 1 would require a corrected disclosure if the APR becomes inaccurate, while Alternative 2 would require a corrected disclosure only if the APR becomes inaccurate beyond the applicable tolerance, or if a fixed-rate transaction becomes an adjustable rate transaction. We recommend, as follows:

- We recommend that the Board adopt Alternative 2, with a modification, for several reasons. Alternative 1 could result in unnecessary and repeated delays in closing that could present inconveniences and other problems for consumers. Since a corrected disclosure requires a three-day waiting period, each correction would require a delay in closing. A change in the APR, within the applicable tolerance, is not a sufficient change in the loan to require such a significant consumer inconvenience.

- Also, Alternative 2, while the better alterative, would be improved by permitting flexibility to waive the three-day waiting period, as discussed next.

In summary, we recommend that the Board require a corrected final disclosure only if the disclosure understated the APR beyond the tolerance, and provide consumers the ability to waive the waiting period.

Consumers May Want to Waive a Waiting Period

There are many cases where a mandatory waiting period could cause unnecessary consumer harm. Some costs are third-party costs that creditors may be unable to accurately predict. Should they change and require a new waiting period, consumers could be in a bind.

A consumer may be purchasing a home under a contract that requires closing by a date certain. Failure to close by that date could cost the consumer a down payment as well as contractual damages. Either could be quite expensive to the consumer. Or, there may be multiple sales that are made dependent on each other, so that if one fails to close, another fails as well. Or, a consumer may have an interest rate lock that will expire during a period of rising rates. In each of these cases, the waiting period could do more harm than good.

Consumers will have a variety of reasons why they may wish to waive the waiting period. Creditors are not able to make a waiver decision for on a consumer's behalf nor do can the Board. Consumers should be permitted to affirmatively waive the waiting period when they wish to do so.

For these reasons, we recommend strongly that the Board permit consumers to request a waiver of the three-day waiting period, in writing, and creditors be permitted to honor those requests.

<u>APR Reduction, Regardless of the Reason, Should Not Require a Corrected TILA Disclosure And a New Waiting Period</u>

The Board discusses the possibility that in the same transaction both of the following occur after the consumer receives a TILA disclosure:

- The consumer selects a smaller principal amount, so that the earlier disclosed finance charge becomes overstated.
- The interest rate increases, so that the disclosed APR becomes understated.

The Board believes an APR is based on an overstated finance charge only where the APR is also overstated. Therefore, the Board would require a corrected disclosure in this case even though the APR was based on an overstated finance charge.[19] We agree that an APR based on an overstated finance charge is accurate only if the APR is overstated.

Under proposed § 226.19(a)(2)(iv), an APR also would be considered accurate if it decreases for specified reasons. We believe that if the interest rate used to calculate the final TILA disclosures is accurate when the final disclosure is mailed or delivered to the consumer, a reduction in the APR, regardless of the reason, is clearly beneficial to the consumer and should not require corrected TILA disclosures and a delay in closing. An APR decrease always benefits the consumer, but redisclosure may not because of the waiting period.

We believe that the applicable APR and RESPA tolerances adequately protect consumers against unanticipated increases in settlement costs at closing. While RESPA tolerance rules provide an incentive not to understate estimates, substantially overstating the disclosures would be such a significant competitive disadvantage that creditors have a very strong incentive to avoid doing so. Concerns that over-disclosures on earlier disclosures will undermine their integrity are misplaced because of the strong competitive pressures against overstating costs.

If an overstated APR will be deemed accurate when the overstatement is based on an overstated finance charge alone, the rule would be uncertain and difficult to apply. In the

[19] 74 Fed. Reg. 43232, 43261(August 26, 2009).

following circumstances, for example, it is unclear whether the overstated APR results from an overstated finance charge:

- A settlement charge included on the final TILA disclosure was included in the prepaid finance change when it should have been excluded.
- The estimated amount of a settlement charge included on the final TILA disclosure was properly treated as a prepaid finance charge but the actual charge is waived or reduced.
- A charge that was treated as a prepaid finance charge and was expected to be paid by the borrower when the final TILA disclosure was prepared is paid by the seller and excluded as seller's points.
- The finance charge included within the payment schedule of the final TILA disclosure is overstated because the borrower negotiated a lower rate and the actual fixed rate or initial interest rate on an ARM is lower than the rate used to prepare the final TILA disclosure.
- The prepaid finance charge, initial interest rate, and margin used to calculate the fully indexed rate on an ARM loan have not changed from the final TILA disclosure, but an updated lower index value results in a lower fully indexed rate and causes the finance charges included within the payment schedule of the final TILA disclosure to be overstated.

We recommend that the Board clarify that an overstated APR, regardless of the reason for the overstatement, is considered accurate and that no corrected disclosure, and no new waiting period, is required. Any reduction in an APR benefits the consumer, and a new waiting period is not necessary because consumers do not need protection from benefits.

<u>Proposed Exceptions for Discounts for Title Insurance Discounts or Automatic Debits</u>

- Title Insurance

  Proposed § 226.19(a)(2)(iv)(B) states that the APR will be considered accurate even if there is a decrease in the loan's APR due to a discount a title insurer gives the consumer on voluntary owners' title insurance. However, proposed Comment 226.4(g)-2 states that "premiums for owner's title insurance coverage are not finance charges because they are not imposed as an incident to the extension of credit." If such premiums are not finance charges, how could a reduction in the amount of those premiums result in an overstatement of the APR? Is this exception meant to cover a discount given to the consumer on the cost of the lender's coverage due to the purchase of voluntary owner's title insurance coverage?

- Automatic Debits

  If the final TILA disclosure is prepared before the borrower chooses to obtain a lower rate by arranging for automatic debits, it would appear that the actual APR would be overstated from the APR disclosed on the final TILA disclosure due to an overstatement of the finance charge (the higher finance charge included in the payment schedule). We believe this exception should be covered by the general rule that a disclosed APR is accurate if it results from a disclosed finance charge that is overstated.

Consummation Disclosure

We suggest revising proposed Comment 19(a)(2)(iii)-1 under the Board's Alternative 2 by adding the bold language and deleting the language ~~struck through~~:

> *(If a change occurs **that makes a disclosed term inaccurate but does not require receipt of a corrected disclosure three business days before consummation** ~~that does not render the annual percentage rate on the early TILA disclosures inaccurate~~, the creditor must disclose the changed terms before consummation, consistent with Section 226.17(f).)*

For clarity, we further recommend that § 226.19(a)(iii) should also refer to the requirement to provide disclosures prior to consummation in these cases.

ARMs Where the Initial Rate is Not Determined Using the Index or Formula that Applies to Rate Adjustments

- The proposal retains existing Comment 26.17(c)(1)-10(i) (renumbered Comment 226.17(c)(1)(iii)-3(i)), which states that for an ARM where the initial rate is not calculated using the index or formula for later rate adjustments and the loan contract provides for a delay in the implementation of changes in an index value (a "look-back period"), the creditor may use any index value in effect during the look-back period before consummation in calculating the disclosures. We request that proposed Comment 17(c)(1)(iii)-3(i) clarify that, for disclosures prepared prior to consummation, the creditor may use any index value during the look-back period as of the date the disclosures are mailed or delivered, and that that the final APR to which the previously disclosed APR is compared for accuracy may be calculated with any index value in effect during the look-back period before consummation.

- The proposal retains existing Comment 17(c)(1)-10(iv) (renumbered Comment 17(c)(1)(iii)-3(iv)), which states that these transactions involve irregular payment amounts and are subject to the rate tolerance of ¼ of 1%. We request a further clarification to Comment 17(c)(1)(iii)-3(iv) that these transactions are considered irregular transactions notwithstanding the fact that an index value in effect during the look-back period before consummation may result in a fully indexed rate that happens to equal the initial interest rate and payments that happen to be equal.

V. CONTENT AND FORMAT OF DISCLOSURES

We are pleased that the proposed format requirements, including the requirement to tailor the disclosures to the specific features of the requested loan, are designed to improve consumers' ability consumers to read and understand the disclosures. We very strongly support disclosures that consumers can understand.

However, the format requirements are complex, increasing the risk that a consumer may not understand them or that a creditor may make an inadvertent error. We therefore make several recommendations.

Additional Examples

To help creditors deal with the complex formatting requirements, we recommend that additional disclosure examples be provided which cover, at a minimum, the structure of all of the standard mortgage programs of Fannie Mae, Freddie, Mac FHA, and VA.

The Proposed APR/APOR Graph Is Not Informative to Consumers And Is Overly Complex to Produce

The proposed APR to APOR comparison would be given to consumers early in the application process to illustrate where the consumer's APR falls in comparison to rates on other consumer loans in the same week the disclosure is given. While we certainly agree that consumers should be clearly informed about their interest rates, we do not believe this particular disclosure would be very helpful, as discussed below. At the same time, operationally, it would be extraordinarily difficult to produce because it would require technology the mortgage industry does not have in place. Further, the shading requirement would make the disclosures difficult to read and photocopy in most circumstances. We suggest below other disclosure methods that would provide more timely and useful disclosures with considerable less regulatory burden.

➤ ***The Proposed Disclosure Would Be Hypothetical***

The disclosure would disclose an APR on a graph that compares the range of rates, during the week the disclosure is produced, from the "average best" APR to the APRs in the "high-cost zone." The disclosure would compare the APR to APRs on "similar" conforming loans offered to applicants with "excellent" credit. It would also disclose the amount the consumer's payment would decrease by a 1% point APR reduction.

Because the disclosure would be provided early in the application process, it would be hypothetical because the APR will change before consummation, for a number of reasons.

- With an all-in APR, many, many factors would cause the APR to change after application before closing.
- Market interest rates are always fluctuating.
- The consumer may not yet have decided whether to select an adjustable or fixed rate.
- The consumer may not yet have decided whether to make a larger down payment in exchange for a lower rate, or to do the opposite.
- The loan-to-value (LTV) ratio would not yet be known, yet it can have a significant affect on the APR of a mortgage loan.

The disclosure would lead consumers to believe that their credit score determines their APR. It would compare the APR to applicants with excellent credit and to high-cost loans, "usually available to applicants with poor credit history."

While credit score is one factor that determines a loan's interest rate, it is by no means the only factor. Market interest rates certainly affect the loan rate very significantly. The LTV also can be very significant, yet the disclosure makes no mention of the effect of the LTV. Lien position affects the loan rate but not the APOR. (It does affect the margin added to the APOR to determine the HPML and HMDA reporting thresholds, because lien position is so significant to the loan rate.) Owner occupancy also affects the loan rate. We question whether emphasizing the credit score and ignoring other significant factors would be an appropriate form of disclosure.

At this stage of the loan application process, it may be too late for consumers to be able to improve their credit scores materially. Even if a consumer could do so, it is unlikely that the credit score would improve enough to cause a 1 percentage point decrease in the APR, as the disclosure would show.

- ***The Disclosure Would Require Adopting New Technology***

Loan origination systems are designed to make a number of consumer disclosures, but are not equipped to handle graphic displays such as the proposed graph. The technology in place today can put numbers and characters into particular boxes and locations, but is simply not capable of creating the proposed graph.

Should the Board go forward with the proposed graph, new mortgage origination software would need to be developed and programmed to produce the shaded disclosures. The new systems would then need to be integrated into all the loan origination systems nationwide. This process would need 18 to 24 months to complete, and would be hugely expensive.

- ***Shading May Make Disclosures Illegible***

Shaded text or background would be a particular problem in any mortgage disclosure, even if creditors did bear the expense of equipping themselves to produce disclosures with shading. Shaded disclosures are more difficult to read. This would be especially true where consumers and creditors may need to fax or make photocopies of the disclosures, which could render the text printed on a shaded background illegible. We are concerned about a disclosure that lenders would be unable to fax, and that would be illegible if photocopied.

Given that the disclosure uses a hypothetical or potential APR rather than the APR the loan will actually have, given that the disclosure will become obsolete right away and certainly in a week, and given that the disclosure focuses on credit history over market rates, LTV, lien position, owner occupancy, and other significant factors, we suggest that in this case the cost of the disclosure far outweighs the consumer benefit.

- ***Suggested Alternative Disclosure***

We suggest that a better alternative would be to combine the APOR comparison with a credit score disclosure. The APR to APOR comparison will only be useful if consumers understand how their creditworthiness compares to the creditworthiness of other consumers. We recommend that the Board adopt a disclosure that is generic rather than transaction-specific.

Alternatively or in addition, the Board could post a graph weekly that consumers could use, showing current market rates on a range of relevant loans.

- ***Suggestions if the Board Adopts the Proposed Graph***

If the Board does adopt the proposed graph, we have the following suggestions for improvements and requests for clarification.

- *Revised APOR Calculations to Reflect All-In APR.* Because the APR will now be an all-in APR, the calculation of the APOR should be revised to include the average amount of all of the fees now included in the calculation. Without this change, the comparison of the APR to the APOR will be misleading because the APOR will be understated from the actual average APRs offered to prime customers.

- *Date of APOR.* In proposed § 226.38, paragraph (b)(2) indicates that the disclosed APOR should be for the week in which the disclosure required under this section is "provided" while paragraph (b)(3) says that it should be the APOR as of the date the disclosure is "produced." Since there may be a delay between when a disclosure is produced and when it is provided to the consumer (for example, when a disclosure is produced but mailed the next business day) we request a clarification that the creditor may use the APOR in effect on the date the disclosure is either produced or provided. This would be very helpful because when the disclosure is produced, the creditor may or may not know exactly when it will be provided. Additionally both paragraphs (b)(2) and (b)(3) refer to the higher-priced mortgage loan threshold as defined in § 226.35(a)(1). That threshold is determined using the rate set date. We recommend that proposed Comment 38(b)(3) be revised to indicate that the APOR may be determined as of the date the disclosure is either produced or provided, and to delete the reference to Comment 35(a)(2)-3, because that Comment states that the APOR is determined by the rate set date.

- *Comparison for Loans Not Secured by Owner-Occupied Properties, Loans Above Conforming Loan Limits, and for Loans with LTVs above 80%.* The APOR is computed for owner occupied conforming loans with LTVs of 80% or less. As a result, the APOR substantially understates the average prime offer rate for loans that are not secured by owner-occupied properties, for loan amounts above the Fannie Mae / Freddie Mac conforming loan limit, and for loans with LTVs above 80%. That is, the APOR understates the rate for a significant proportion of loans. We offer two suggestions:

The Board should consider publishing separate APORs for these types of loans so that consumers will see an accurate comparison.

We recommend revising the language used to explain the comparison by adding the bold language and deleting the language ~~struck through~~:

> *How does this loan compare? For the week of (date) the average APR on similar {but* ***smaller****} conforming loans offered to applicants with excellent credit* ***and substantial equity in their homes*** *was ___%. Today an APR of ___% or above is considered high cost and is usually ~~available~~ charged to applicants with poor credit history* ***or whose loan amounts are very large or are more than 80% of their home's worth.***

<u>Format Errors Should Not Give Rise to Statutory Damages</u>

We recommend that the Board clarify that failure to comply with format requirements should not give rise to statutory damages.

<u>Top of Form</u>

- ***Address***

The borrower's mailing address may be different than the address of the property securing the loan. We request clarification that both addresses may be shown.

- ***The Number of Loan Officer Unique Identifications***

Proposed Comment 38(g)(2)-1 would require that where there are multiple originators, the unique identification numbers of all originators be listed. However, many loans may have five or six individuals who are registered as loan originators touch the file indirectly. Tracking every originator who touches a loan file, however indirectly or superficially, would be a significant regulatory burden with little or no apparent consumer benefit.

We recommend that, for loans with no broker, no more than one loan originator be required to be disclosed. If there is a broker, we suggest requiring disclosure of one loan originator from the creditor and one from the broker. Additionally, we recommend permitting creditors to use any reasonable method of determining which loan originator to list. For example, the loan originator who takes the application, who the consumer will deal with directly, should be a reasonable and satisfactory disclosure.

- ***Loan Type – Rate Reduction Mortgages***

There are rate reduction mortgage products where the loan's rate will decrease by specified amounts at specified times if the loan is paid as agreed. We request a clarification that these loans should not be disclosed as step rate mortgages. Step rate mortgages are defined by proposed § 226.38(a)(3)(i)(B) as loans where the interest rate may "change" after consummation and the rates and periods in which they will apply are known. We recommend that the word "change" be revised to "increase." This would be consistent with § 226.38(a)(3)(ii)(A), which requires a step rate disclosure if rates will "gradually increase."

<u>Total Settlement Charges and Itemization of Amount Financed – Conforming TILA and RESPA Requirements</u>

➢ ***Disclosure of Total Settlement Charges on Final Disclosure***

Proposed Comment 226.38(a)(4) provides that for the final TILA disclosure, the creditor may disclose the sum of "Charges That Cannot Increase," "Charges That In Total Cannot Increase By More Than 10%," and "Charges That Can Change." It appears that the total that will be shown on Line 1400 of the HUD-1 or HUD-1A may not be used. Presumably this is because Line 1400 may include amounts such as real estate broker fees that were not disclosed on the GFE and are not a cost of the loan. If this is the intent, the Comment should state that the Line 1400 total may not be used.

The Comment further indicates that the creditor has the alternative for the final TILA disclosure of providing the consumer with the final HUD-1 or HUD-1A. In all of the model forms provided in the Proposal, however, the Total Settlement Charges disclosure appears in the Loan Summary section and is not bracketed. If the creditor provides the final HUD-1 or HUD-1A, the creditor should have the option of either making or not making the Total Settlement Charges disclosure on the final TILA disclosure. The Board should also include within the model forms a final TILA disclosure that does not include the Total Settlement Charges disclosure because the final HUD-1 or HUD-1A was provided.

➢ ***Requirement to Provide GFE with Early TILA Disclosure Should be Eliminated When Processing Broker Provides the Initial GFE***

The Board's proposal would permit the GFE to substitute for the Itemization of Amount Financed when provided with the early TILA disclosure. Where the creditor provides the initial GFE, this presents no problems.

However, where application is taken by a processing broker (rather than a table funded broker) the processing broker will usually send the initial GFE to the borrower within three business days after the broker receives the application, and the creditor will usually send the early TILA disclosure in a separate package within three business days after the creditor receives the application. We recommend that in these circumstances the broker's provision of the GFE in accordance with RESPA requirements be deemed to satisfy the Itemization of Amount Financed requirements.

➢ ***Requirement for No Estimates and HUD-1 with Final TILA Disclosure***

The Board states that "the Board believes that to permit substitution of the HUD-1 settlement statement for the itemization without requiring that it be delivered three business days before consummation would be inconsistent with the purposes of the MDIA amendments."[20] We respectfully disagree. First, nothing in the Mortgage Disclosure Improvement Act (MDIA) restricts the use of estimates on TILA disclosures given prior to consummation. Second, the MDIA only requires redisclosure and a new waiting period if the APR becomes inaccurate. Thus, MDIA recognizes that disclosures may reflect estimates and that the closing should not be delayed because the final disclosures may be somewhat different than the estimated disclosures.

As noted above, if the Board intends to have the total settlement charge disclosure on the final TILA disclosure not be an estimate and will not permit the HUD-1 given at settlement to substitute for the Itemization of Amount Financed, then the Board should require the closing agent to finalize all fees and provide the HUD-1 to the creditor at least eight business days prior to closing. Otherwise, the Board should permit estimates that are consistent with RESPA's tolerance requirements. The Board should also permit the HUD-1 itemization given at consummation to satisfy the requirement to itemize the amount financed.

➢ ***Revise Itemization of Amount Financed to Be Consistent With Other TILA Disclosures***

Under the Board's proposal, creditors would continue to have the option of providing an Itemization of Amount Financed, but the TILA disclosures will not refer to prepaid finance charges and will highlight the loan amount more prominently than the amount financed. We recommend that an additional model form for the Itemization be provided for use with closed-end mortgage loans. The new form should be an itemization of the disbursements from the loan amount, which would not contain a disclosure of the amount financed or prepaid finance charge.

➢ ***Prepayment Penalty Disclosures***

We address a number of factors that require clarification concerning prepayment penalty disclosures.

- Circumstances of Penalty on HOEPA and HPML loans. We recommend that model language be provided on how to disclose the limitations on the assessment of prepayment penalties under §§ 226.32 and 226.35.

- Two-Stage Penalty Calculation. We request that in situations where the use of the two-stage penalty calculation is permissible, creditors be given the option of disclosing the actual maximum prepayment penalty.

[20] 74 Fed. Reg. 43232, 43314 (August 26, 2009).

- Incorporate into Official Commentary That Prepayment on FHA Loans Mid-Month is Not a Penalty. Proposed Comment 226.18(k)(1)-1 lists as an example of a prepayment penalty "Charges determined by treating the loan balance as outstanding for a period after prepayment in full and applying the interest rate to such 'balance'." This Comment appears to be inconsistent with Comments 226.36(c)(1)(i)-1 and 2 and the explanation of these comments provided by the Board[21] on the required prompt crediting of payments. Those comments and the explanation noted that (i) many loans require calculation of interest based on an amortization schedule where payments are deemed credited as of the due date, whether the payment was actually received prior to the schedule due date or within any grace period, (ii) the rule requiring crediting of payments as of the date of receipt was not intended to prohibit or alter the use of the monthly accrual amortization method, and (ii) the crediting the payment as of the payment due date was not considered to be the imposition of additional interest.

  In a letter dated September 29, 2009, after publication of the Board's proposal, the Board clarified that lenders that use such an interest accrual method that accepts a prepayment mid-month but charging interest through the next scheduled due date is not an assessment of a prepayment penalty for any purpose under Regulation Z.

  We recommend that the clarification the Board provided in that letter be incorporated into Proposed Comment 18(k)(1)-1, that for FHA loans and other loans on the monthly accrual amortization method, crediting a prepayment as of the next installment due date is not considered to be additional interest after prepayment in full and is not a prepayment penalty. Should the Board decide that such situations should be considered prepayment penalties then we request that the Board also clearly note that this change is prospective only.

<u>How Much Could I Save By Lowering My APR?</u>

As the Board acknowledges, although this disclosure refers to a lowering of the applicant's APR by 1 percentage point, the actual calculation, as explained in proposed § 226.38(b)(4), would be based upon a reduction in the interest rate, rather than APR, by 1 percentage point. It is also unclear why the model form has a blank for the amount of the reduction in the APR if 1 percentage point should always be used.

We recommend that the disclosure be revised to state

> *How much could I save by lowering my interest rate? For this loan, a 1 ~~%~~* ***percentage point*** *reduction in the ~~APR~~* ***interest rate*** *could save you an average of $______each month.*

Alternatively, if the Board determines that to use the APR in the disclosure, in addition to the calculation method contained in the proposal the Board should also permit the savings to be calculated using the same methodology that is used to reduce payments to cure an APR violation.

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[21] 74 Fed. Reg. 43232, 44571 (August 26, 2009).

We also note that the examples only address fully amortizing loans with monthly payments. We request that the Board provide an example of how the disclosure was calculated for the balloon loan shown in form H-19(D). We further suggest the Board publish model language for loans that do not require monthly payments.

Treatment of Escrow Payments

- Under the Proposal, if the creditor requires the establishment of an escrow account, then the escrow payments must be included in the Interest Rate and Payment Summary. The rationale is that many consumers compare loans based on the monthly payment amount. However, while it makes sense for consumers to understand the amount that they will need to set aside for taxes and insurance each month, they will need to set aside the same amount, regardless of whether an escrow account is established. As the Board's HPML rules recognize, it is often in the consumer's benefit to have an escrow account. Requiring that the average monthly amount of taxes and insurance be disclosed only on loans where an escrow account will be required may be misleading. Also, it would facilitate an unscrupulous loan originator comparing its payments without escrow to the consumer's existing loan, or a competitor's new loan, that includes escrow.

  We recommend that for all first lien loans, the Interest Rate and Payment Summary should include the Estimated Tax and Insurance amounts whether or not an escrow account is required.

  For subordinate loans, the creditor should have the option of either estimating the taxes and insurance amounts, or of disclosing that the taxes and insurance are not included in the disclosures. Escrows on subordinate loans are rare, and the subordinate lender may not know what the consumer pays for escrowed items.

- Disclosure should accommodate the possibility that some but not all items are escrowed. When an escrow account is required, some items may be paid out of the escrow account while other items are paid directly by the consumer. However, the Escrow language for loans that require escrow accounts in the "More Information About Your Payments" section of the disclosure does not appear to take this possibility into consideration, although the GFE and HUD-1 do. We suggest revising the language by deleting the language ~~struck through~~ and adding the language that in bold as follows:

  > *An escrow account is required~~ for property taxes and insurance (such as homeowner's insurance)~~. Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for ~~more~~ details **on what property taxes, insurance (such as homeowner's insurance) and other items will be paid from the escrow account and which items you must pay on your own.***

- Disclosure for Key Questions About Risk and payment increases. We request a clarification to the requirements of § 226.38(d)(1)(ii) that, on a loan with an escrow account, the possibility of an increase in the escrow payment will not trigger this disclosure. The consumer bears the risk of an increase in the cost of property taxes and insurance whether or not the consumer obtains a loan or has an escrow account.

Introductory Rate Notice And Discounted Initial Rate

When the initial interest rate on an ARM loan is not set by using the same formula that will be used for rate adjustments, the creditor will not know at the time that the early TILA disclosure is prepared whether the initial rate chosen by the borrower will be higher or lower than the fully indexed rate at the time of consummation. This is because the index value used to compute the fully indexed rate may increase or decrease between the time the early TILA disclosures are prepared and consummation.

For example, assume that at the time the early TILA disclosure is prepared the initial interest rate is 6.00% and, based upon an index value of 3.00% and the margin of 2.75%, the fully-indexed rate is 5.75%. At consummation, the initial interest rate is 6.00% and, based upon an updated index value of 3.375% and the margin of 2.75%, the fully-indexed rate is 6.125%.

We recommend a clarification to Comment 226.38(c)(2)(iii)-1 that the creditor should determine whether to provide the introductory rate notice on early TILA disclosures and any revised TILA disclosure given prior to the final TILA disclosure based upon an estimate of the fully-indexed rate, using an index value no older than the look-back period as of the date the disclosure is mailed or delivered to the consumer.

Disclosures Required When Loan Assumed by "Subsequent Consumer" Should be Limited to Situations Where Subsequent Consumer Was Not Obligated on the Loan, Was Not an Owner of the Property, and is Purchasing an Interest in the Property

The proposed revised Comment 226.2(a)(24)-1 on the definition of residential mortgage transaction removes the reference stating that the definition was relevant to the § 226.20(b) disclosure requirements for assumptions. Section 226.20(b) continues to indicate that an assumption requires new disclosure if the assumption is by a "subsequent consumer." The proposal would delete Comment 226.20(b)-2, which does clarify when assumption disclosures are required. This leaves no definition of subsequent consumer and no reference to a residential mortgage transaction, so it is not clear when new disclosures would be required.

We recommend that new disclosures only be required if a consumer who was not obligated on the original loan and was not already an owner of the property purchases an interest in the property. There are many situations when there has been a transfer of an interest in the property. Also, the Garn-St Germain Depository Institutions Act of 1982[22] prohibits acceleration of the loan under a due on sale provision. In these cases, one of the original

[22] 12 U.S.C. 1701j-3, implemented in 12 C.F.R. Part 591.

borrowers will ask to be released from personal liability on the loan and servicer will agree to such release if the other individual agrees to be personally liable and is creditworthy. However, the Garn-St Germain Act does not require servicers to provide such releases. If servicers are now required to provide assumption disclosures in these circumstances, then they may not decide not to entertain such requests.

Clarifications in Model Forms

- ***Percent or Percentage Point***

The APR disclosure, in the model forms, says "For this loan, a __% reduction in the APR could save you an average of $___ each month." The regulation, § 226.38(b)(4), requires disclosure of "a 1 percentage **point** reduction in the APR." The form needs to be revised to match the regulation, by adding the word "point." A one percentage point reduction in the APR, such as from 8% to 7%, is a 12.5% reduction in the APR, not 1%.

This change is needed in the Adjustable Rate Loan Program Model Form, Adjustment Notices, and in the APR disclosures on the model forms.

- ***Unless a Cap Applies***

The Adjustment Notices do not accommodate the possibility that a cap may limit a future rate increase, which is important information. We suggest the adding the following language in bold:

> We could have increased your interest rate another ___ % but did not because a rate cap applied. We can add this to your interest rate when the interest rate adjusts again on (date) **unless a cap applies**.

Separate Disclosures Required by Proposed § 226.38(j)

The Proposal notes that the rebate, late payment, property insurance, contract reference, and assumption disclosures were not of primary importance to consumers and were not always well understood. Even if these disclosures are provided in a separate form, they will still contribute to information overload. We therefore recommend that these disclosures be eliminated entirely. It is not the purpose of the TILA to require consumer disclosures that do not benefit consumers.

If the Board does retain them, we recommend:

- The Board should not expand the current assumption disclosure requirement to disclose whether a loan is assumable from purchase transactions to all mortgage loans. As Board noted, "very few participants understood the language indicating that the loan was assumable, and even fewer felt it was important information."[23]

[23] 74 Fed. Reg. 43232, 43313 (August 26, 2009).

- It should be sufficient to provide the disclosures once at any time prior to consummation.

<u>Disclosures In Languages Other Than English</u>

The Board solicits comment on issues concerning disclosures in languages other than English. CMC members do provide non-English disclosures. However, we do not believe creditors should be specifically required to provide disclosures in languages other than English. The costs and litigation risk would be extraordinarily high. Different translators may translate the same language in different ways, making each translation subject to risk.

We believe it is important that disclosures be as clear and as consistent as possible. If the Board were to require creditors to provide non-English disclosures, each creditor would provide a differently worded disclosure than each other creditor. We believe this would be rather confusing to consumers, especially if they are attempting to shop among lenders. We believe the far better approach would be for the Board to provide its model forms in each language needed. This would ensure consistency and clarity, and would ensure that the disclosures meet legal requirements. Further, the forms would be available on the Board's website for consumers to access.

VI. PROHIBITING LOAN ORIGINATOR COMPENSATION BASED ON LOAN TERMS AND CONDITIONS

We agree with the Board that loan originator compensation should not adversely affect the loans that consumers obtain. We support the proposed prohibition on loan originator compensation based on loan terms, subject to the clarifications listed below.

We note that the Board proposes § 226.36(d) under the Board's authority under TILA § 129(l)(2), which permits class actions and statutory damages for very minor and technical violations. This exposes lenders to the risk of hugely expensive litigation, sometimes frivolous litigation. We therefore urge the Board to make the rules as clear as possible.

<u>General Issues</u>

- ***Loan Originator Definition***

The definition of "loan originator" should exclude individuals who are managers and supervisors, whose compensation is not based upon loans that they directly originate, but on the production of the individuals they manage and supervise. Managers and supervisors have little actual impact on an individual loan, so their compensation arrangements do not raise the same concerns about incentives to encourage consumers to obtain inappropriate loans. We suggest the Board restrict the compensation arrangements only of those individuals who regularly deal with consumers directly and who have the ability to set, negotiate, or decide loan terms or loan amounts. The compensation restrictions should not apply to those who only process loan applications because they do not have the ability to set, negotiate, or decide loan terms.

- ***Loan Amount***

Compensation based on loan amount should be permitted. In addition to compensation based on a fixed percentage of the loan amount subject to a minimum or maximum that was discussed in the proposal, it should also be permissible to use percentages that decrease as the loan amounts increase. To address the Board's concern that larger loan sizes may increase LTVs, lower the consumer's equity, and increase risks, we recommend that the final rule permit lower compensation for higher LTVs.

We note that is particularly important that creditors be able to consider loan amount in the compensation they pay to brokers. While there are a number of ways that creditors and mortgage brokers may be able to compensate their own employees in a way that may be financially viable without directly considering loan amount, (such as considering the loan originator's overall volume) the inability to consider loan amounts could cause severe distortion in the mortgage broker market. Furthermore, HUD would likely view compensating a broker based upon the broker's overall volume as a violation of § 8 of RESPA.

- ***Loan Originator Volume***

We request clarification that the ability to consider the loan originator's "overall volume" includes not only the number of loans but the total dollar amount of loans. This amount is too attenuated from individual loans to affect loans individually.

- ***CRA Loans***

Additional compensation should be permitted for Community Reinvestment Act (CRA) loans, defined as loans to low- and moderate-income (LMI) consumers and loans secured by property in LMI census tracts. This is important because CRA loans can be much more difficult to originate than other loans,

- ***Certain Commonly Used Compensation Criteria Should Not Be Loan Terms or Conditions***

We request clarification that compensation may be based upon pull-through rates, file quality, customer satisfaction, and communication quality. Lenders need these common sense management tools.

- ***Amounts Not Retained Should Be Excluded From Definition of "Compensation"***

The definition of loan originator "compensation" should be clarified to exclude any amounts that are not retained by the loan originator, such as amounts that are used to pay closing costs.

- ***Concessions Should Be Permitted to Affect Compensation***

We recommend that an employer should be able to reduce the loan originator's compensation for granting a concession. This will permit reasonable flexibility in unusual circumstances.

- ***Broker's Receipt of Compensation from Both Creditor and Consumer Should Not Be restricted if Total Compensation is Reasonable***

In many transactions, both the wholesale creditor and the consumer will be making compensation payments. The proposal provides no guidance on how to determine in these situations whether broker compensation is being paid by the creditor, the consumer, or both.

It would be preferable to allocate payments in a manner consistent with the RESPA rule and eliminate the restriction on receipt of compensation from both the creditor and the consumer when the broker's total compensation is reasonable. This would allow creditors to compensate brokers in a manner similar to how they compensate retail loan originators they employ, without violating RESPA.

- ***Creditor Payments Should Be Allocated Consistently With RESPA***

Consistent with how creditor payments will be disclosed on the GFE and HUD-1 under the final RESPA rule, we recommend that payments by creditors (after netting with any payments made by the broker to the creditor) be first allocated to broker compensation and then to a credit to other closing costs. The consumer should not be considered to pay discount points in a transaction with creditor-paid broker compensation.

- ***If Total Broker Compensation Does Not Exceed Agreed Upon Amount and is Reasonable, Brokers Should Be Allowed to Receive Payments From Both Creditor and Consumer***

We recommend that if the creditor and the broker agree upon an amount of total broker compensation that is not based upon the transaction's rate or other terms and conditions and that does not exceed reasonable amounts of compensation, the broker may receive compensation from both the creditor and the consumer that does not exceed the agreed upon amount. We suggest that total broker compensation be deemed reasonable if it does not exceed 2% of the loan amount, subject to a minimum of $500.

> **Examples** - Assuming that the broker and wholesale creditor A agreed that the broker would receive compensation of 1% from the creditor for rates of 5.500% or higher, wholesale creditor A could also offer a rate of 5.375% and pay the broker .5 points and the broker could also receive .5 points from the consumer, because the 1% total broker compensation does not exceed reasonable charges.

On the other hand, if the broker and wholesale creditor B agreed that the broker would receive compensation of 3%, then because that amount exceeds what is reasonable, the broker could not receive compensation from both the creditor and the consumer. Because payments would be allocated in a manner consistent with RESPA, wholesale creditor B might offer a rate of 6.125% at which it would pay all of the broker's 3% compensation or the consumer could be offered wholesale creditor B's rates of par (5.250%, for example) or below with the consumer paying all of the broker's compensation at whatever amount the broker and consumer agree upon.

APR to APOR Comparison – If the concern is that consumers will not know that they are paying too high a price for a loan due to excessive broker compensation, that concern could be addressed by prohibiting a broker from receiving any compensation from a creditor unless at the time of the GFE the broker provides a disclosure comparing the transaction's APR to the APOR in the format required by § 226.38(b) (or arranges for the creditor to provide the early TILA disclosure within three business days of the broker's receipt of the application from the consumer).

Steering

We agree that prohibiting payments from creditors to brokers based on loan terms and conditions would be meaningless if brokers could significantly increase their compensation by steering the borrower to another creditor.

The proposed rule would define prohibited steering based on what is in the "consumer's interest." It would state that there is no steering if the consumer selects a loan from "three loan options for each type of transaction in which the consumer expressed an interest," and the loan originator meets several other requirements, including a requirement to supply a number of options for loan types in which the consumer "expresses an interest" and for which the loan originator has a good faith belief that the consumer "likely qualifies." However, compliance with the proposed rule would be extraordinarily burdensome. The proposed rule uses vague terms that are not readily susceptible to any definition, let alone actual implementation. It would also require burdensome tracking requirements. We suggest that the Board could address its concerns in a manner that would entail significantly less uncertainty and less regulatory burden.

We suggest that the anti-steering rule should not apply to transactions where the broker's total compensation (not just creditor-paid compensation) is reasonable. We suggest that total broker compensation be deemed reasonable if it does not exceed 2% of the loan amount, subject to a minimum of $500. By exempting transactions where total broker compensation is reasonable, it is unlikely that consumers will be inappropriately steered due to compensation considerations, and the risks and operational burdens of brokers will be greatly reduced.

➢ ***Focus on Total Broker Compensation, Not Creditor-Paid Compensation***

It is not clear why it should be permissible for a broker to steer a consumer to consummate a transaction in which the consumer will pay direct broker compensation that is greater than amounts that are reasonable, particularly if the loan amount is increased so that the consumer may pay the broker's compensation from loan proceeds. We believe the rule should focus on whether the broker is steering the consumer to consummate a transaction in order to receive greater total broker compensation than could have been received on other transactions the broker could have offered.

➢ ***Employees of Affiliates in Compliance With Anti-Steering Rules***

Proposed amendments to § 226.36(d)(1) would prohibit loan originators from receiving compensation based on a loan's terms or conditions, and it would treat affiliated entities as a single person.

Proposed § 226.36(e)(1) is similar. It prohibits loan originators from "steering" consumers to loans on which the loan originator would greater compensation, unless the loan is in the consumer's interest. While similar, proposed § 226.36(e)(1) does not state how it would treat affiliates.

Proposed Comment 226.36(e) states that a loan originator who is a creditor's employee and who complies with § 226.36(d)(1) also satisfies the requirements of § 226.36(e)(1). We recommend an analogous clarification for employees of a creditor's affiliate. Loan originators who comply with § 226.36(d)(1) should be deemed in compliance with § 226.36(e)(1) if they are employees of the creditor's affiliate.

VII. DISCLOSURES AFTER CONSUMMATION

Adjustment Notices

➢ ***Timing of Adjustment Notices***

We support changing the minimum period of time that an adjustment notice must be provided before a payment change from 25 days to 60 days. However, exceptions should be provided for existing loans with look-back periods shorter than 45 days, and construction and temporary loans, as below.

➢ ***Existing Loans With Short Look-Back Periods***

Consider an FHA loan that will have a rate adjustment on February 1 and a payment adjustment on March 1. Sixty days prior to March 1 is December 31. FHA loans have a 30-day look-back period, so that the index value used to determine the new rate is the index as of January 2. It is impossible to send a rate adjustment notice on December 31 reflecting a January 2 index value. In any case, servicers need time after the index value becomes available to perform quality control checks before mailing the notices.

- ***Recommended Exception for Existing Loans With Short Look-Back Periods***

For adjustable rate loans with application dates prior to the effective date of the revised regulation, and that have look-back periods shorter than 45 days, the adjustment notice should be provided within 15 days after the look-back date, but not less than 25 days prior to the payment change.

- ***Construction and Temporary Loans***

These products should continue to be exempt from the requirements to provide adjustment notices. The concern that borrowers have sufficient time to refinance before the payment increases is not relevant in these circumstances because it is highly unlikely that the consumer would be able to refinance a construction or bridge loan prior to completion of construction or the sale of the house. Construction loans and bridge loans often have adjustable rates with short or no look-back periods. Imposing the longer look-back period may cause creditors not to offer these products.

Content and Format of Adjustment Notices

- ***Combining With Other Required Notices***

We request a clarification that servicers may combine the adjustment notices with other disclosures, such as disclosures required by law, or disclosures that are required by Fannie Mae, Freddie Mac, the Federal Housing Administration, Veterans Administration, or Rural Housing Service, unless expressly prohibited by law.

- ***Prepayment Penalty Disclosure***

The proposed ARM adjustment forms require disclosure of the amount of a prepayment penalty. This disclosure is difficult to make accurately, which we believe is a problem. The amount of any prepayment penalty can vary for a number of reasons, all of which are difficult to incorporate into a short, clear disclosure form. For example, the amount of a penalty may vary based on whether the consumer sells the home or refinances the loan. Further, any calculation would necessarily be based on an assumed principal balance, which may or may not be inaccurate. We recommend that the disclosure state that:

> *If you pay off your loan, refinance or sell your home before (date) you could pay a penalty. Call us to find out the amount.*

- ***Description of Interest Rate***

The language provided in Model Form H-4(G) indicates that "Your rate will change due to an [increase] [decrease] in the (index)." This language does not appear to take into consideration the following situations:

- The current and new rates are the same;

- The old and new index values are the same; or
- The current rate is a premium or discount rate so that the change in rate if any, is not entirely due to a change in the index value (or may be directionally different if the amount of the premium or discount exceeds the amount of the change in the index).

Because it is possible for the rate to remain unchanged, or to change in part independently of the index, we believe it would be more accurate to discuss the change in the index rather than the change in the rate. We suggest the following disclosure:

> *The index on your mortgage [increased] [decreased] [stayed the same], which may affect the interest rate.*

- ***Allocation of Principal, Interest, and Escrow On Interest Only and Negative Amortization Loans***

Providing an allocation of the current and new payment between principal, interest, and escrow on interest only and negative amortization loans is a substantial compliance burden. Since the notice must also include a Disclosure of New Monthly Payment that includes the amortizing payment as shown in model clauses H-4(H), it is also unnecessary. Moreover, because escrow payments may also be in the process of adjustment according to RESPA requirements, providing correct escrow information may be difficult. Providing escrow information would also be confusing if the escrow changes will occur at a different time than the loan payment change, which is a very common occurrence.

Escrows and escrow disclosures are governed by RESPA. RESPA escrow rules provide thorough consumer protections. There does not seem to be a need for TILA disclosures to duplicate RESPA escrow disclosures, especially when doing so would likely confuse consumers.

- ***Conversion to Fixed Rate***

Where an adjustable rate loan is converted to a fixed rate loan under a written agreement, no adjustment notice should be required because the consumer will already have received disclosures about this event.

Statement Requirements for Negative Amortization Loans with Payment Options

The proposed negative amortization monthly disclosure model form is certain, or almost certain, to be inaccurate and misleading. It simply does not take into consideration all the permutations on these types of loans. For example, it would tell consumers that if they make their minimum payment, their principal balance will increase. This is not necessarily true. The minimum payment amount may be based on a different loan interest rate than applies to newly accruing interest. The outstanding principal could increase or decrease. Payment-option loans are not feasibly handled by a one-size form.

A better solution would be to require the proposed form to be used only on loans that are originated after the final rule becomes effective. The number of loans affected by that time would likely be extremely small. This would greatly reduce the number of inaccurate or misleading consumer disclosures. Existing loans continue to be covered by the interagency guidelines on nontraditional mortgage products.

Creditor Placed Insurance

We support the proposed requirements, but make the following suggestions.

- A Comment should be added clarifying that all references to the "creditor" in this section refer to the creditor or the servicer performing these functions for the creditor.

- The proposal would require a creditor to make a reasonable determination that the property insurance has lapsed before placing insurance. However, the rule needs to permit servicers to comply with pooling and servicing agreements, under which the servicer is contractually obligated to obtain insurance if the consumer has not documented that there is sufficient insurance coverage in place.

- Servicers may be contractually obligated to obtain insurance, even if the coverage has not lapsed, because the coverage is insufficient.

- Importantly, the proposal would permit a creditor to charge the consumer retroactively for insurance. This is important because consumers are contractually obligated to maintain adequate insurance coverage at their expense.

- The Proposal asks whether the notice should include a local or toll-free number to contact the creditor regarding creditor-placed insurance. We agree that the contact information included in the notice should include such a local or toll-free number.

VIII. SUGGESTIONS FOR CONFORMING RESPA AND TILA

Pre-Application Disclosures

Mortgage brokers should provide TILA's pre-application forms prior to application or collection of any fee. These disclosures include:

- "Key Questions to Ask About Your Mortgage"
- "Fixed vs. Adjustable Rate Mortgages"
- Adjustable Rate Loan Program Disclosures for programs in which consumer expresses an interest.

Conforming TILA Disclosures and GFEs

Consumers would greatly benefit from coordinated TILA disclosures and GFE "Summary of Loan" and "Escrow Account Information" sections.

One alternative would be to require all loan originators to provide TILA disclosures and replace the Summary of Loan" and "Escrow Account Information" sections of the GFE with a cross-reference to the TILA disclosure. This would help consumers understand the interplay between the two sets of disclosures.

Providing a TILA disclosure would be a new requirement for processing brokers, but they possess all of the information necessary to provide the TILA disclosure. It would be useful for consumers to have this information earlier in the process.

A second alternative would be for processing brokers to use a different form than creditors, and require processing brokers to have the creditor mail or deliver early TILA disclosures to the consumer within three business days after the broker receives an application from the consumer.

- ***Creditor Form***

The first form would be used by creditors under TILA (including table-funded brokers), which would be the same as the GFE under the first alternative discussed just above, cross-referencing the TILA disclosures provided by the creditor.

- ***Processing Brokers***

We recommend that processing brokers who are not creditors under TILA be required to provide, or that the creditor provide, the early Regulation Z disclosures and the GFE, within three days of receipt of an application.

Revise GFE Blocks and HUD-1 To Reflect TILA's Proposed All-In APR

If the Board does adopt an all-in APR, it will need to be coordinated with the GFE and HUD-1. The all-in APR includes in the calculation of the APR all charges the borrower incurs because of the loan. It excludes charges that the borrower would have incurred had the property been purchased for cash, such as the owner's title and the cost of preparing and recording the deed. The GFE and HUD-1 would need to similarly distinguish between charges incurred as part of the purchase transaction from charges incurred because of the loan. Making this distinction will make it much easier to reconcile the GFE and HUD-1 with the TILA disclosure.

Conform Treatment of Amounts Paid by Parties other than Borrower

The proposed new TILA disclosure requires the disclosure of "Total Settlement Charges" as shown on the HUD-1. However, RESPA rules are not clear about whether this amount will reflect the only the amounts that the borrower will pay. There are ambiguities in the RESPA treatment of amounts paid by the seller, a builder, an employer or the broker or creditor. We believe these should be clarified and coordinated.

Conform Timing Rules and Waiting Period Requirements

- ***HUD-1 Three Business Days Before Consummation***

Because a consumer must receive a final TILA disclosure at least three precise business days before consummation, the borrower should also receive the final HUD-1 at the same time. The closing agent should also be required to finalize all fees and charges at least eight business days prior to closing and provide that information to the creditor in order for the creditor to provide an accurate final TILA Disclosure. All of the fees for the closing agent and for the services of third parties arranged by the closing agent should be disclosed as the closing or settlement fee on Line 1102 of the HUD-1, other than amounts that are disclosed as part of the title insurance premiums.

- ***Redisclosure Requirements***

Loan terms and APR should be disclosed on TILA disclosures under TILA rules, rather than on RESPA disclosures under differing rules. TILA rules and not RESPA rules should govern redisclosures for increases in the APR, beyond tolerances. Other changes should not require TILA redisclosure, even if they require a revised GFE.

RESPA's requirements to provide a revised GFE should apply only to change in settlement costs beyond the applicable tolerance, not to a change in loan terms.

The timing of both TILA and RESPA redisclosures should be reasonably coordinated.

These improvements would reduce the number of disclosures that are duplicative in substance but differing in form, thereby improving the clarity and value of all the disclosures.

- ***Waiting Period***

RESPA may require that fees be reduced in order to stay within tolerance. Reductions in fees or in interest rates after the final TILA disclosure should not trigger requirements for an additional corrected TILA disclosure and should not require a new waiting period.

Settlement Cost Booklet

On December 16, 2009, HUD published a Settlement Cost Booklet that is designed to help consumers shop for a mortgage loan. It discusses the new RESPA forms in detail but does not discuss the TILA disclosures. We believe all disclosures about the same transaction should be complementary, and should be integrated into one set of forms. We urge HUD and the Board to design their disclosures and their disclosure requirements together.

IX. PAPERWORK REDUCTION ACT AND EFFECTIVE DATE

We note that the Board estimates:

> The Board estimates that 1,138 respondents regulated by the Federal Reserve would take, on average, 200 hours (five business weeks) to update their systems, internal procedure manuals, and provide training for relevant staff to comply with the proposed disclosure requirements in §§ 226.38 and 226.20(d), and revisions to existing disclosure requirements in §§ 226.19(b) and 226.20(c). . . . On a continuing basis the Board estimates that 1,138 respondents regulated by the Federal Reserve would take, on average, 40 hours a month to comply with the closed-end disclosure requirements[.][24]

We respectfully submit that this estimate is extremely low.

The notice of proposed rulemaking runs almost 200 *Federal Register* pages. Just reading the proposal, let alone understanding its implications, took days. Preparing this comment letter required assembling a team who then worked on this project for over four months. Once the final rule is published, the industry will then have to implement the rule, which will then reasonably take at least 24 months.

There are a number of different loan origination technology systems across the industry, as well as within individual companies. Implementing Regulation Z amendments will require each revision to be programmed, implemented, and then tested, separately in each of these origination systems. Changes to loan origination systems must be made in a coordinated fashion because each change can impact other changes that are being designed and made simultaneously. Coordination itself is a labor-intensive task.
For some perspective, we note that at one large lender, implementing the Regulation Z amendments that became effective October 1, 2009 required over 70,000 hours. Implementing the recent amendments to Regulation X took twice that amount of time, and those rules are still changing. Implementing the present rulemaking will likely require more resources than the October 2009 rulemaking but less than Regulation X.

If the Board does finalize the APR/APOR comparison with shaded text and a graph, the regulatory burden would increase greatly. That single item presents the largest technology challenge of any part of the proposed rule. We urge the Board to revise that disclosure, as discussed above.

We request the Board consider the implementation challenges the rulemaking will have on the industry, and recommend that the Board give the industry at least 24 months to implement the final rule.

[24] 74 Fed. Reg. 43232, 43318 (August 26, 2009).

X. CONCLUSION

The CMC appreciates the Board's proposed rule to improve the quality and effectiveness of consumer mortgage disclosures through out the loan application process and through the life of the loan. The proposed all-in APR is intended to make the APR disclosure more useful, but would create a number of issues. In particular, we are concerned that it would constrain credit in states where the laws are based on TILA and Regulation Z terms. We do not believe the Board meant to curtail credit, but that will be the unintended result of the proposal. If the Board does adopt an all-in APR, we suggest some ways to address the problems that will arise. An all-in APR would also require a number of clarifications about the revised definition of "finance charge."

We appreciate the clarity in the new model forms for TILA disclosures. We do suggest ways to make them even clearer. We also suggest more clarity concerning compensation restrictions.

Finally, we suggest some ways the TILA disclosures and RESPA disclosures can be more closely coordinated.

Thank you for your time and consideration of our views.

Sincerely,

Anne C. Canfield
Executive Director